REPORT ON THE BUSINESS ENVIRONMENTAL STRATEGIC TASKFORCE AIR COMMITTEE FACILITATED DISCUSSIONS ON NEW SOURCE REVIEW REFORM

Presented to Tennessee Department of Environment & Conservation Commissioner Betsy Child

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PURPOSE OF REPORT

This report presents the views from members of the Business Environmental Strategic Taskforce (BEST) Air Committee who participated in facilitated discussions during the summer of 2004 on how the State of Tennessee might revise its air pollution rules concerning New Source Review (NSR). The Committee offers it as advice to the State in framing a draft rule. The report does not necessarily represent the views of all BEST members concerning the content of a final rule. Moreover, while this report looks at five major proposed areas of change in the NSR rules, there are additional changes and details that the group did not address in depth. The Committee hopes, however, that this report will offer a constructive starting point for promulgating a rule.

Tennessee Department of Environment and Conservation (TDEC) Commissioner Betsy Child urged the environmental and industrial communities to develop a mechanism for better dialogue and communication. BEST was established in the fall of 2003 to encourage open discussion and cooperation among parties interested in environmental regulation and conservation in the State. BEST includes, but is not limited to, representatives from industry and environmental advocacy groups. BEST has several committees including an Air Committee.

This report offers industry and environmental community perspectives on the NSR reform issue. Specially, the report addresses the federal NSR rule issued in December 2002 by the Environmental Protection Agency (EPA). Under the federal rule, states such as Tennessee that have State Implementation Plan (SIP)-approved NSR programs have three years to submit a SIP revision to EPA to address the federal rule.

The report does not contain a consensus model rule. All parties recognized that a consensus on recommended rule language for the Tennessee Air Pollution Control Board (Board) to propose or adopt was beyond the realistic scope of the discussions, given the limited timeframe, complexity of the issues, and the widely divergent and deeply held views of the participants and larger stakeholder groups. Furthermore, to encourage candid discussion and a good faith effort to identify general areas of agreement and disagreement on NSR reform, the parties met with the understanding that their efforts would not be used in any way to influence the federal litigation over the EPA NSR rules. Furthermore, no position taken by a participant would be admissible as evidence in an agency proceeding or court case related to the Clean Air Act. The participants engaged in a constructive dialogue that went beyond broad policy viewpoints. Specifically, through the discussions, the parties identified many areas of the federal rule where there is general agreement and where industry and the environmental community differ in only minor respects. The parties also identified some areas of agreement with respect to points that should be addressed in the State NSR rule that are not included in the federal rule. The

discussions also identified where respective positions are more divergent. It is intended that this report on the facilitated discussions on NSR reform will be a useful resource for the Department and the Board as they consider rulemaking to respond to EPA's request for a SIP revision to be submitted by January 2, 2006.

BACKGROUND

- In December 2002, EPA adopted a final rule that makes changes to the NSR regulations that apply in "prevention of significant deterioration" (PSD) and nonattainment areas. On the same day the final rule was issued, EPA proposed additional rule changes to address how "routine maintenance, repair and replacement" projects were to be evaluated.

- Thirteen states and the District of Columbia along with environmental and public health groups have challenged the federal rule in the District of Columbia Circuit Court of Appeals. A number of states also have intervened on the side of EPA in support of the rule.

- The NSR Reform Rule consists of five major components:
  - Clean Units;
  - Pollution Control Projects;
  - Method for Determining Baseline Emissions;
  - Actual-to-Projected-Actual Methodology for Determining Whether a Project Will Cause Air Emissions Increase; and
  - Plantwide Applicability Limits.

- Under the federal rule, states with SIP-approved NSR programs such as Tennessee, have three years from promulgation to submit a SIP revision to EPA to address the federal rule. EPA's rule requires states to adopt the rule as "minimum program requirements" by January 2, 2006 to maintain EPA approval. States are not required, however, to adopt the federal rule exactly as it was promulgated by EPA. States may adapt and modify the rule to meet particular state

needs, provided the state rules are at least as stringent as the federal rule. EPA has not provided guidance as to how it will determine whether a state rule is at least as stringent as the federal rule.

- In early 2003, industry requested TDEC to move expeditiously to undertake a state rulemaking process to adopt the federal rule. The environmental community expressed opposition to proceeding with such rulemaking changes.
- In early 2003, at the request of Commissioner Child, representatives of environmental and industrial communities began a dialogue through BEST on NSR reform.
- In August 2003, EPA issued a second NSR reform rule addressing the equipment replacement and repair provisions of the rules. This rule was challenged by some states and environmental groups and was stayed by the U.S. Court of Appeals for the District of Columbia Circuit in December 2003. (The court had previously declined to stay the federal rule issued in December 2002.)
- In part because of the stay, the BEST Air Committee participants agreed that discussions on NSR reform would focus only on the December 2002 federal rule and not the stayed August 2003 rule.
- In January 2004, TDEC held a series of town-hall meetings to hear public viewpoints on NSR reform of those present. Businesses, industry, and some local officials supported expeditious adoption of the EPA rule by TDEC. Representatives of the environmental and public health communities opposed adoption.
- In the spring of 2004, Commissioner Child offered to retain facilitators to help foster the BEST Air Committee's discussions.
- In an effort to further the discussions among the parties, the facilitators recommended that a small group of industry and environmental group representatives from the BEST Air Committee conduct the discussions and report back to and solicit input from their respective BEST Air Committee members.
- The facilitators convened the representatives, who were self-selected by the environmental groups and industry, for a series of meetings between June and September. The discussion focused on an evaluation of each of the five components of the December 2002 federal rule in an effort to find areas of consensus and, where consensus was not possible, to provide clarity on how the views diverge.
- A draft of this report was prepared and circulated by the representatives who participated in the discussions to the rest of the BEST Air Committee members and, in some cases, additional

stakeholders. Due to time constraints and other factors, the report does not fully incorporate the views and concerns expressed by those parties in response to the draft of this report.

GENERAL PRINCIPLES

As a threshold matter the participants agreed on several overarching principles:

- Tennessee needs healthy air and a healthy economy.
- The leaders in the State of Tennessee, within and outside of government, should embrace a comprehensive policy for air quality that brings all sectors of the State together in working towards these goals.

Regarding the specific impact of the NSR rulemaking the participants agreed:

- Taken as a whole, the rulemaking changes should be environmentally neutral or beneficial when compared with the rule currently in place in Tennessee.
- The State should seek to have efficient and effective NSR rules, and if aspects of the current rules add needless complexity or delay, the rules should be improved, provided that air quality in Tennessee is not harmed.

CLEAN UNITS

Summary of EPA Provision: This provision adds an applicability test for emissions units that are designated as Clean Units. The federal rule provides that when a unit has gone through Best Available Control Technology (BACT) or Lowest Achievable Emission Rate (LAER) review, or can demonstrate that it has controls comparable to BACT or LAER, a source may make any changes at that unit without triggering additional NSR, if the change does not require a change in the emission limit or other requirement that was part of the BACT/LAER determination. Thus, provided an emissions unit maintains clean unit status, any emissions increases that occur from the emissions unit as a result of a project at the source are not considered in determining whether the project is a major modification. Clean Unit status is automatic and is valid for up to 10 years from the date that the technology was installed or three years from issuance of the NSR permit provided certain conditions are met. In nonattainment areas, the federal rule may allow emissions units that were previously required to install BACT, rather than LAER, to be designated clean

units for up to 10 years. There is a mechanism to renew that designation if the Clean Unit test is still met.

- Areas of General Agreement: Both sides agree that as a general matter the Clean Unit provision can be a viable mechanism for improving the State's NSR rule and providing some additional incentive for a source owner to install controls on units that can reduce emissions.
- Clean Controls. The environmentalists believe that a source should qualify for Clean Unit status on the basis of controls that have been certified as BACT or LAER, which is a clearer standard than on the basis of controls that are deemed "comparable to" BACT or LAER. Industry believes that it is clear how to demonstrate that a unit's control technology is comparable to or substantially as effective as BACT or LAER.

POLLUTION CONTROL PROJECTS (PCPs)

Summary of Provisions: This provision codifies, with certain changes, an EPA policy that addresses industrial source projects that substantially reduce emissions of an NSR pollutant, but that may cause increases in another NSR pollutant above significant levels. For utilities, the PCP exemption was incorporated into the federal rules in 1992. The PCP provision applies only in those instances where installation of one pollution control measure will increase emissions of a second pollutant (*e.g.*, an incinerator to destroy volatile organic compound (VOC) emissions or hazardous air pollutants (HAPs) to comply with a maximum achievable control technology (MACT) standard while incidentally increasing oxides of nitrogen (NO_x) emissions). The PCP provision is designed to ensure that there is not a disincentive to install pollution control technologies.

To encourage PCPs that will have a net environmental benefit, the federal rule replaces and expands in some respects the policy guidance and existing utility rule with a single uniform PCP rule. The final rule specifically identifies certain projects that are presumed environmentally beneficial and presumptively qualify as PCPs. The federal rule also details the mechanism by which non-listed projects may be deemed pollution control projects and addresses related matters, including reporting and notices. The rule, unlike EPA's preexisting policy, does not require that in order to qualify as a PCP the primary purpose of the project must be pollution control. If a pollutant increases above significance levels the permitting authority must assure that the increase will not cause or contribute to a violation of any national ambient air quality standard or PSD increment or adversely impact Air Quality Related Values in Class I areas (*e.g.*, national parks).

- Areas of Agreement: The parties agree that as a general matter PCPs are valuable and should be encouraged. They also agree on

several clarifications as outlined below that are appropriate to be included in the State NSR rule that are not specifically included in the federal rule.

- Rebuttable Presumption: The federal rule includes a list of projects that presumptively qualify as PCPs. The parties agree that the State NSR rule should specifically clarify that the State can rebut this presumption for a project when the State has evidence that the project would harm the environment.
- HAP Increases: In response to the environmental community's concern about otherwise beneficial projects that would increase HAPs, the parties agree that, unlike the federal rule, the State NSR rule should specifically provide the State with authority as part of its "environmentally beneficial" review of projects to consider the impact of any hazardous air pollutants that are associated with the PCP itself.
- Offsets: The parties agree that the State NSR rule, unlike the federal rule, should specifically clarify that emission reduction offsets must be provided for any PCP in a nonattainment area that would result in a significant net increase of a nonattainment pollutant.

BASELINE ACTUAL EMISSIONS

Summary of Provision: This provision addresses the way in which sources (other than electric utility steam generating units, or EUSGUs) determine "baseline actual emissions" for three discrete purposes: when calculating "pre-change" actual baseline emissions in determining whether a proposed project will increase emissions under the "actual-to-projected-actual methodology;" when setting a cap for a PAL; and when used in netting to determine creditable emissions increases/decreases. The provision allows a source to average emissions during any consecutive 24-month period during the 10-year period prior to the change to determine baseline. If a single unit is involved, sources may use a different consecutive 24-month period for each NSR pollutant in evaluating a project. If multiple emissions units are involved, the source must use the same 24-month period for all units. EPA's prior rule generally used the previous two years (while allowing other periods to be used if shown to be more representative of normal operating conditions).

The rule does not affect the emissions calculation method for utilities, which will continue to use the highest two years during the previous five. The federal rule requires that sources adjust their baselines downward to exclude noncompliant emissions during the baseline period and that the baseline must be adjusted for certain sources to reflect current emissions limitations imposed after the baseline period. The federal rule includes fugitive emissions and

emissions associated with startups, shutdowns, and malfunctions in the baseline emissions.

- Areas of Agreement: The federal rule methodology for determining the baseline emissions for netting, PALs, and the emission increase test is probably the aspect of the federal rule on which the parties have the most divergent views. There was agreement, however, that the State rule should not include a particular point (Pollutant-Specific Baselines), discussed below, that is included in the federal rule.

- Look-Back Period: The environmental community recognizes that industries do go through economic swings, including downswings, and some flexibility in setting baselines may be in order. It believes, however, that the long look-back period may be used to inflate the baseline above current actual emissions, thereby allowing projects inappropriately to evade NSR. The environmental groups are comfortable with the approach taken in the current State rule and prior federal rule. Under the current rule, the presumptive look-back period is the two-year period immediately preceding the change. The environmentalists believe that rule provides ample flexibility, however, because it allows a source owner to demonstrate that another two-year period would serve as a "more representative" baseline. Industry states that its experience is that it is frequently difficult and time consuming to demonstrate that a period beyond the current two–year baseline period is more representative of normal operations. With the caveat that many in the environmental community remain unconvinced that any change from the two-year look-back is warranted, the environmental community expressed willingness to discuss alternatives to the new federal rule, such as:

  - An average ton/year emission rate over the 10-year period; or
  - Any two consecutive years during the past five years, with discretion to look back an additional five years if granted by TDEC. This approach follows the approach currently used for EUSGUs but allows for additional flexibility.

  Industry strongly supports the approach taken in the federal rule and does not believe that any alternative approach would be acceptable, except that it would prefer to average emissions during any consecutive 12-month period, rather than 24-month period, during the 10-year period prior to the change to determine the baseline. Industry's view is that all businesses go through business cycles where plant outputs vary and emissions should not be deemed to increase when plant output (and resulting emissions)

falls within these business cycles. Thus, the rules should effectively "net out" fluctuations in the business cycle retrospectively.

- Pollutant-Specific Baselines: Environmental groups are concerned that the federal rule allows sources to select different 24-month periods for each regulated NSR pollutant. Industry agrees that the State rule could include a provision that states that the baseline must be the same two-year period for all pollutants and units, provided the rule includes the 10-year look-back.

ACTUAL-TO-PROJECTED-ACTUAL TEST

Summary of Provision: The second provision addressed by EPA in determining how to calculate whether a proposed project will cause an increase in emissions is the actual-to-projected-actual method. "Actual" was addressed above with baseline issues. "Projected actual" is a determination of projected post change emissions. Historically, EPA's rule provided that when calculating post-project emissions, a plant's potential to emit should be used unless the plant has already begun normal operations. Under the new methodology, a source may project future actual emissions as the maximum emissions that will occur in any one of the five (and in some cases ten) years after the change. This provision is similar to the rule that has applied to EUSGUs since 1992. In calculating projected emissions after the change, the source looks at the historical utilization and emissions and tries to determine increases that may occur as a result of the project itself, not increases the unit was capable of accommodating before the project, including any demand growth that could have been accommodated earlier. The federal rule does not provide the permitting authority with the opportunity to review projects before they are constructed and does not make the projected emissions levels enforceable limits. The federal rule requires non-EUSGU sources to submit reports to the permitting authority only if post-change emissions increase by a significant amount and are in excess of the pre-change projections.

- Areas of General Agreement: While the environmental community was satisfied with EPA's prior actual-to-potential test, both parties generally agree that the actual-to-projected-actual test is acceptable in concept. They also agree that certain points can be included in the State NSR rule that are not addressed in the federal rule, as outlined below (Transparency/Notice/Comment). The environmental groups have several concerns with the test as it is set out in the new federal rule. These are discussed below (Demand Growth).

- Transparency/Notice/Comment: The parties agree that in the State NSR rule, unlike the federal rule, it is appropriate to require an administrative mechanism that provides an opportunity for transparency with respect to the emissions calculations made by

sources in evaluating whether a project increases emissions without hindering a source's ability to initiate a project. This mechanism should focus attention on projects that have a reasonable possibility of resulting in a significant net emissions increase. If net emissions at a source increase, the environmental community would like the mechanism to include timely notice and opportunity for TDEC to review the methodology and conclusion that NSR is not triggered. The business community would like the mechanism designed to avoid project delays.

- Demand Growth: The environmental community believes that the "demand growth" exclusion is inappropriate in that it will allow unit emissions to increase. It believes any significant increases in emissions should require imposition of BACT-level or LAER-level controls. It also believes that because it is impossible to uniformly distinguish between emissions increases that are attributable to a growth in demand and those that are attributable to a physical or operational change to the source, the demand growth exclusion will allow units that should impose controls to argue that they are merely experiencing demand growth. Industry believes the demand growth exclusion is absolutely necessary, appropriate, and required by the language of the statute (to be counted, emission increases must be caused by a project and not by independent causes). Industry believes that the abundant monitoring and record keeping requirements currently in place make determining demand growth emissions fairly straightforward.

PLANTWIDE APPLICABILITY LIMITS (PALs)

Summary of Provision: PALs allow sources to manage emissions under a plantwide cap. Previously, the federal rules did not have specific provisions on PALs and their relationship to NSR.

The PAL provision included in the federal rule is an "actuals" PAL. Under this rule, if a source agrees to take a plantwide emissions limit as its actual emissions rather than as its permitted allowable emissions, it will gain added flexibility to change operations without undergoing NSR review. The source can add new emissions units, modify units, or increase emissions at some units and decrease at others, as long as the PAL is not exceeded. The PAL is set by using the baseline methodology discussed earlier (*i.e.*, under the new federal rule a source can look back 10 years and select the highest 24-month period to set the PAL emissions levels). PAL limits are established after a public comment process. The federal rule contains additional provisions regarding record keeping and monitoring to provide the permitting authority and public with information to monitor PAL compliance. The PAL mechanism precludes a

source from making a series of unrelated emissions increases that fall just below PSD trigger thresholds, which it currently can do under the existing state rules. The federal rule does not require that the source commit to any decrease in emissions from the facility over the 10-year effective period of the PAL.

- Areas of General Agreement: Both sides generally agree that the PAL provisions offer a mechanism to induce sources to limit their existing authorization to emit (i.e., the emissions between actual and allowable permit levels). Additionally, both sides generally agree that an actuals PAL creates an incentive for sources to use further controls in order to maintain maximum flexibility under the PAL.
- Baseline: A key concern of the environmental community is how the "actuals" limit is determined. These concerns are detailed under the discussion of "baseline emissions" but apply here as well.
- Limits on "Bad Actor" Participation: A second concern of the environmental community is that regulated entities with a history of violations should not be allowed to take advantage of the PAL provision in the federal rule. Specifically, they suggest that the State rule should contain a "bad actor" provision that allows the State to preclude those with a history of violations of the Clean Air Act from using a PAL and obtaining the benefits associated with it. Industry strongly objects to including such "bad actor" provisions in the State NSR rule for the following reasons: bad actors are unlikely to use PALs; the federal rule's record keeping requirements will allow the State to monitor compliance with the PAL and take appropriate enforcement action, including revocation of the PAL; it will be very difficult to define "bad actors;" the issue is not addressed in the old NSR rules or new rules and should be beyond the scope of the State rule as well and instead should be addressed in another context, if at all. The environmental groups respond that this is precisely the context in which limits to the PAL concept should be considered and implemented, that defining "bad actors" is the type of issue that is entirely appropriate for TDEC to address, and that to rely on the record keeping provisions of the federal rule makes little sense when bad actors can be identified upfront and prevented from using PALs.
- Declining Caps: The environmental community believes that declining caps would be valuable and justified in nonattainment areas. The environmental community also believes that at a minimum the State NSR rule should require that the emission caps in PALs be established at levels representative of historic actual levels, as discussed above in the context of Baseline Actual Emissions. Industry believes that the State should decide how

nonattainment areas achieve air quality goals on an area-by-area basis in the SIP, and that there should not be automatic declining caps in PALs.